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Harmonization and Globalization of Commercial Law

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Current international private law (PIL) developments through mid-2001

Private international law (“PIL”) projects, including unification or harmonization of commercial law, necessarily build on comparative law and practice but seek to go beyond that to reach international standards through negotiations. The general purpose, unlike that of the public law, is to adopt legal standards that can be used by private parties in cross-border commerce to structure transactions, assess legal risk, and enforce rights or obligations directly in national courts or through arbitration. International PIL negotiations also serve to clarify both black-letter and transactional differences between legal systems, point up the extent to which economic developments and business practices can be reflected through this process, and clarify issues relevant to business credit and country risks in the various negotiating countries.

Public law negotiations on related trade matters, by way of contrast, generally focus on market access issues, rather than on rules useable for particular transactions, avoid comparative law issues to the extent possible, and provide for rights enforceable generally through some form of governmental process, whether national or international (such as the WTO, NAFTA, ICSID, etc.). Public trade law for example might focus on opening market access for certain banking and financial services, as is done under NAFTA and authorize cross-border activities, without dealing with contract or other terms and conditions of cross-border banking practices, and usually without requiring parity or commonality between applicable legal systems. Related private law projects, by contrast, in the banking and financial services area in recent years have covered harmonization of bank guarantee and letter of credit law by treaty, international credit transfers, uniform treaty standards for modern negotiable instruments, and more recently efforts to upgrade international private law for secured financing.

Set out below are a selection of current developments on commercial law projects sponsored by international governmental bodies. While many depend on participation by and important preparatory work of private sector groups, implementation often, but not always, requires some measure of governmental sanction to create commercial predictability for cross-border transactions. As a preliminary comment, the first two categories below were, as recently as the mid-1990’s, at the top of the “impossible” list, that is areas of law so divided by country differences and established traditions so as to render efforts at harmonization out of the question. The reasons why the first two areas of the law now are on top of the U.S. list of achievable efforts, which include but are not limited to globalization, will be expanded on orally.

International Commercial Finance

This topic leads the list because 2001 will be an unusual year in this field. Traditional wisdom assured us as recently as the mid-1990's that secured finance law reform was wholly impractical, given the wide divergences between country laws and even the purposes such laws served. Yet, now by the end of this year three international projects on secured financing are likely to be completed, which will set the stage for possible implementation by the U.S. and other countries either by treaty enactment, legislation or promotion by trade and other associations. A fourth project has begun, and two more are on the immediate horizon. All share some commonality from the U.S. vantage point, i.e. if properly completed they will reflect and promote modern commercial finance and capital markets standards. This means avoiding the more traditional method of harmonization, i.e. the balancing of existing legal systems, and using instead financial benefits and efficiency of the commercial law as benchmarks. The extent to which this can be accomplished will be a reflection of the extent to which globalization continues to strongly affect world attitudes in the coming year.

UNCITRAL: Convention on accounts receivable financing

This potentially far-reaching convention is based on economic principles, already reflected in the UCC and the laws of some countries, and not simply harmonization of existing laws on assignments. The convention will cover international assignments as well as domestic assignments of cross border receivables, and will permit assignments of non-possessory and future interests, as well as "bulk" assignments, all of which are cornerstones of modern commercial finance. Perfection and priority, on which consensus on a single rule could not be reached, is determined by applicable law pointers which permit transaction structuring, by resting on the location of the assignor for most purposes, and the location of the debtor for certain provisions which affect the debtor's rights. The connection with insolvency law is also dealt with by applicable law pointers. Additional provisions override most anti-assignment clauses, provide a limited proceeds rule, and set out optional standards for conflict of laws rules. Optional provisions for priority rules keyed to a notice filing registry system, and a treaty basis for a future computer-based international registry are set out in an annex, along with alternative priority rule systems currently employed by some countries.

The final text was completed at the 2001 UNCITRAL plenary session in June/July in Vienna, with approval by the UN General Assembly expected in December 2001.

UNIDROIT: Draft convention on mobile equipment finance

Parallel in many respects to the UNCITRAL convention, the UNIDROIT convention focuses on asset-based finance, also reflected in the UCC (Articles 2A and revised 9). The draft convention provides for the creation of an international interest which would prevail over otherwise valid local interests to the extent covered by the convention. Each type of equipment

will need a separate negotiated protocol. The first protocol on aircraft equipment is expected to be completed along with the basic

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convention. Additional draft protocols are already in preparation for rail and space equipment, and other equipment categories may follow.

Unlike the UNCITRAL convention, it provides at the outset for establishment of an international notice-filing registry for perfection and priority, and includes provisions on remedies and undertakings as to timeliness, as well as optional provisions on remedies and insolvency rules which, if selected by ratifying states, would enhance credit capacity for covered transactions.

The convention and the ICAO-UNIDROIT protocol on aircraft is expected to be completed in November 2001 at a diplomatic conference in South Africa. Efforts are already underway to develop an international registry prototype, which potentially can set a precedent for industry association-based treaty implementation, and when implemented can set the stage for comparable international computer-based registries for other treaties.

OAS: Model Inter-American Law on Secured Financing and Cross-border Loan Agreements

At the Sixth OAS Specialized Conference on Private International Law (CIDIP-VI), scheduled for November 2001 at Guatemala City, the text of a new and far reaching Inter-American model law is expected to be approved. Carrying an OAS imprimatur, such a model national law if it tracks modern finance standards may be promoted by the IADB, the World Bank and others, which could lead to sufficient adoption to change the financing landscape in the Americas. Even short of such implementation, the conclusion of such an OAS model may lead to changes in existing laws and accepted practices. The draft text covers creation, validity and enforcement and is compatible with current modern secured financing. Following a drafting meeting of 12 OAS states in Miami last November, a new draft of the model law is expected by September 2001, drawing in part on recent legislative developments in Mexico and principles prepared by the National Law Center for Inter-American Free Trade (NLCIFT) at Tucson, Arizona. This text is also expected to include proposed enabling rules for electronic commerce in order to facilitate implementation of the model law.

Hague Conference: Draft convention on law applicable to securities intermediaries

Begun recently in January 2001, this project is an effort to fast-track an agreement on rules on choice of law and applicable law with regard to the movement of and custody of holdings of dematerialized securities, generally reflecting principles in UCC Article 8, and held as collateral by securities intermediaries. The expansion of this commercial mechanism in a number of countries has considerably increased the potential for cross-border use of collateral, enhancing opportunities for investment, credit extension and transactions, but raising at the same time both transactional risk and systemic risk concerns, given the current absence of agreed international rules both on applicable law and substantive law.

In order to fit 1990's legal concepts, at least in some countries, of computer-based rights in securities holdings, tentative consensus has been reached on the so-called

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"Prima" rule for applicable law, centered on the location of the relevant intermediary, and not on older *lex situs* or "look through" rules. Agreement on matters such as the location of accounts or dematerialized securities, however, which would be a key factor in determining *ex ante* the applicable law, has proved so far quite difficult. U.S. and many industry participants want as close to a full party autonomy rule as possible, in part because of the often rapid movement of securities and accounts in computer format, while a number of EU participants and some others favor a more restrictive nexus requirement to any choice of law. The manner in which this issue is resolved will determine whether the proposed treaty system will have value. Consultations with industry, governmental regulators and others are expected to continue through the fall, and if the gap can be closed, the next meeting at the Hague may take place in January, 2002 and may advance to governmental negotiations later in 2002.

UNCITRAL: International Project Finance

UNCITRAL completed in July 2000 a multi-year project on a Legislative Guide for privately financed infrastructure projects. An important mechanism for major projects, especially in developing countries, it reflects a movement away from bilateral and multilateral government funding and control and toward greater reliance on private sector financing, development and operation of a variety of infrastructure needs, from ports and roads to power and public facilities. In order to secure capital market finance, a balance is required between longer term financing and management, greater assurances of rights to obtain adequate returns and repatriate proceeds, and still achieve a balance with project country regulation and specification of public services. The Guide covers legislative frameworks, award of concessions, project risks and government support, financial arrangements, disputes and other matters.

Meetings took place at Vienna in July on possible future work, followed by approval at the UNCITRAL plenary session of a new project on legislative guidance to begin late this September. The leading proposal on the table is to expand the work done on selection of concessionaires, including model provisions.

UNCITRAL: Future work on a UN secured financing model law

After extended debate, the Commission agreed in July 2001 to initiate work on a model law focused on financing of commercial goods, including inventory financing. Notwithstanding approval at the same session of the potentially far-reaching Convention on Receivables Financing, a number of delegations expressed caution about further UN imprimatur on similar modern financing laws, which would go further by potentially dealing with priorities and enforcement. The IMF, the World Bank, the ICC, the EBRD and others supported the new

project, along with the CFA and other industry based NGO's (Non-government organizations represented in these meetings, which now includes the ABA).

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Insolvency law reform

Bankruptcy law reform in the last several years has been recognized by many institutional parties such as the World Bank, the IMF, the Asian Development Bank and others as a front-line issue for both improving access to capital markets, providing access to restructuring financing, and limiting systemic risk. The status and functioning of bankruptcy systems thus are now important factors in both transactional and country risk assessments, and have a direct bearing on commerce and credit ratings, especially in major developing country. Resisted by many as a topic for harmonization in the mid-1990's, progress has moved ahead in recent years.

U.S. Bankruptcy bill and the UNCITRAL Model Law

Included in the Bankruptcy Reform Bill now pending in Congress is a new chapter 15 on cross-border insolvency cases, which would replace existing sections 304, 305 et seq. Chapter 15 essentially adopts the UNCITRAL Model Law on Cross-Border Insolvency approved by the UN General Assembly in 1997, and covers access of foreign representatives and administrators to initiate or participate in proceedings, recognition of main proceedings, limited automatic stays, equal treatment for foreign and domestic parties, authorization for cross-border cooperation between administrators and courts, and other matters. Passage of the bill has been held up for two years because of controversy on consumer provisions unrelated to the cross-border chapter. It is hoped that adoption by the U.S. will lead other countries to consider similar action (Mexico has already done so).

UNCITRAL: Preparation of a UN legal guideline and model provisions for cross-border and domestic insolvency reform.

Following a successful completion of the 1997 UNCITRAL model law on procedural aspects of cross-border insolvency, the U.S., the ABA, the IBA, Insol and a number of international finance bodies have supported further work by UNCITRAL towards preparation of a legal guide for substantive insolvency law reform. A December 2000 Colloquium in Vienna included commercial sector groups, insolvency practitioners and the judiciary, and set the stage for preparation of working documents on which an unexpected degree of initial consensus was by a Working Group on Insolvency Law of approximately 50 countries, NGO's and others at the UN in New York, whose deliberations concluded earlier this week.

Topics covered included access to proceedings, opening of proceedings, operation of stays, different approaches to secured financing rights, role of creditors' committees, directors

rights and liabilities, avoidance powers, and other matters. Much greater recognition of reorganization and refinancing as an option, together with initial acceptance of changes to otherwise applicable standards often necessary to permit such developments, resulted from the meeting, which indicated a significant shift of opinion over the last several years. Included in this change was placing the proposals put forward by the U.S., the ABA and others for additional options for “accelerated

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procedures” clearly in the main text and as a lead-in to the new chapters on reorganization. These procedures, modeled to some extent on “pre-packs” in U.S. bankruptcy practice, would allow pre-agreed workouts for money debt, with capacity to bind holdouts, to proceed without delay and with limited stays and accelerated court supervision.

Parallel to, and responsible in part for this work, has been the preparation of reform proposals by the IMF, the World Bank, the Asian Development Bank and other IFI’s. A revised UN text will be available in September 2001 for comment and will be again taken up by the Working Group in December 2001 and May 2002. This project could bring significant benefits to many countries, as well provide some hedge against systemic risks in countries where absence of an efficient legal system for recycling assets has been a factor in serious economic downturns in recent years.

Non-governmental projects: ALI, IBA, INSOL, III

Each of these organizations has underway efforts to develop new rules or studies and other efforts to promote harmonization or bankruptcy reform. The ALI has produced a three-country effort involving Canada, the U.S. and Mexico which resulted in publication of up-to-date surveys of bankruptcy practice as well as law for each country, and is pursuing areas of possible harmonization. The other organizations referred to are involved in the UNCITRAL Working Group discussed above.

Electronic Commerce

While clearly a modern technology, law and commercial practice field, globalization in other respects has not produced the same degree of commonality nor promoted harmonization. This in part may reflect uncertainties in assessing how law changes impact markets and commercial practice, especially in the absence of a track record in the markets, as well as wide differences between the U.S. and the EU, as well as others, on a range of matters such as the degree to which governments should regulate the new field, or conversely enact only minimal enabling rules (the U.S. approach in large measure), as well as differences on rights in data, commercial vs. privacy rights, software licensing rights, electronic signatures and related matters.

1996 UNCITRAL Model Law on Electronic Commerce

The Model Law, negotiated with U.S. support, contains enabling provisions intended to validate actions using electronic communications in commercial transactions, and rules on computer equivalents to written signatures, originals, etc. While adopted several years ago, it is referred to here because it has been used as a basis for many national laws, including provisions in U.S. federal and state law, and referred to directly in the recently enacted Federal e-signature. An exception to that has been the few provisions on attribution and presumptions, which although drawn from earlier laws on electronic funds transfers, have for the most part been seen within the U.S. as not appropriate for general commercial transactions, until an established track record for e-commerce is achieved and

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the effect of such provisions can be anticipated. Congress has stated that relevant provisions of the Model law should be the basis of further negotiations internationally.

UNCITRAL: Model law on electronic signature and message authentication systems.

This project, underway for several years and controversial, was completed at the 2001 July plenary session. Initially modeled on earlier PKI-based legal concepts, the U.S. had continued to express concern about lack of technology neutrality, rules that could invite over regulation, and provisions on liability. Substantial improvements were made over the last year, including revisions to the liability rules sought by the U.S. While more improvements could have been made, given the likelihood that most states will not adopt the U.S. minimalist approach, the text now may represent a better model for those countries who have not yet adopted e-signature laws than other leading models, such as the EU Directives.

The Model law began with a focus on the then leading applications of digital signature technology, which, while a very important technology for certain purposes, in the view of some should not be a standard for general commercial communications. Related disputes are reflected in domestic differences within the U.S., as seen in the different approaches in recent legislation such as UETA, UCITA, the Federal “E-signature” Act, and earlier state legislation such as the Illinois statute.

Future E-commerce work.

Putting the several last years’ conflicts on e-signatures behind, decisions were made several weeks ago in July at UNCITRAL on proposals for new E-com work, based on the recommendations of the E-Commerce Working Group which met in March. Priority will be given to international rules on formation of contracts, which would cover tangible goods but defer work on “virtual” goods, until more consensus can build up on how to treat the intersection between traditional sales and commercial laws on the one hand, and intellectual property rights, including rights in data and software licenses on the other. While not tied at this stage to the UN’s Vienna Convention on contracts for the international sales of goods (CISG), the relationship will have to be worked out, which potentially may raise issues recently confronted by NCCUSL and the ALI on e-com legislation and proposed revisions to UCC Article 2.

Other leading projects approved but not on the same priority were interpretative agreements or other methods of revision of a potentially large number of existing conventions or bilateral arrangements to reflect new e-commerce realities, and rules on transferability of rights by cross-border computer systems.

UNIDROIT: New E-Com provisions for the UNIDROIT Principles for International Commercial Contracts

The UNIDROIT “Principles”, released in 1995, have found wide application in cross-border contract practice and in commercial arbitration, as a neutral substitute for conflicting national contract laws. The “Principles” draw both from common law and

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civil law, and reflect many developments in the UCC as well. Provisions cover formation, validity, performance and non-performance, damages, etc. This product has contributed significantly to harmonization, although it is noted that partly in response a separate document on European Principles has been in preparation.

UNIDROIT is now at a preliminary stage in its project to add new chapters, including sections on assignments, third-party beneficiary rights, e-commerce and other matters. While provisions on assignments would hopefully draw on the recent conventions and international texts concluded this year, given the uncertainties noted above on e-commerce, achieving consensus on e-rules which support commercial transactions may be a challenge.

Possible work on on-line dispute resolution for the internet and other computer media may also be considered as a joint effort with the UNCITRAL Working Group on international commercial arbitration, which will be covered in a separate report on PIL developments on dispute resolution, including the status of the draft Hague Convention on jurisdiction and enforcement of foreign judgements.

International Franchising

UNIDROIT: Draft model national law on international franchising

The Institute completed in 1998 a Guide to International Master Franchise Agreements, the first such international product in the field. Using that as a basis, UNIDROIT held its first intergovernmental meeting at Rome in June 2001 on a new draft model national law on franchising disclosures in cross-border arrangements. Unlike most of the projects described herein, which generally seek agreement on default rules that can govern the substance of transactions, the preliminary draft model law, which was prepared by a group of private sector experts, is expected to apply only to pre-sale disclosures by franchisers to prospective franchisees.

The proponents do not seek to apply its provisions to the substantive relationship between franchisor and franchisee, nor to third parties. Most countries, as well as many states of the U.S., have little specific regulation of the franchising relationship. This is an example where disharmony on substantive rules has not been shown to create dislocation of the market, unlike the absence of agreed rules on sales of goods. Absence of disclosure rules, however, has been seen as a potential pitfall, as franchise operations and especially franchise investment are taking on a global cast. Although completion has been seen as possible in 2002, it is too early to assess that until a second meeting is convened at Rome in the Spring 2002. Differences have emerged between countries which seek only minimal general obligations of disclosure, leaving many standards to be determined by applicable law, and others such as the U.S. which seek more fully articulated standards and exceptions, which arguably would enhance certainty and transparency across borders.

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Transportation of goods

OAS: Draft uniform bill of lading and rules for Inter-American shipments.

Agreement on an Inter-American uniform bill of lading for overland transportation of goods will be sought this November at the OAS-sponsored Sixth Specialized Conference on Private International Law (CIDIP-VI) to be held in Guatemala City. The U.S., acting as Chair of the CIDIP drafting group, has compiled practices from a number of OAS states which will be circulated in September along with draft rules.

Various models have been used for the proposed rules, including new draft private sector rules developed for road shipments between the NAFTA states, developed by industry representatives from Canada, the U.S. and Mexico under the auspices of the North American Surface Transportation Committee of the National Law Center for Inter-American Free Trade (NLCIFT) at Tucson, Arizona. In view of the wide disparity between both law (including civil law and common law) and transportation practices in the three countries that had to be overcome, either by substantive rules or applicable law pointers, the draft North American road bill of lading may be a starting format for Inter-American issues. The draft rules would also draw on the earlier 1989 CIDIP-produced Convention on overland transportation of commercial goods.

If completed in November, discussion may begin on possible expansion of the harmonization project for a second phase. In order to be of value to all regions of the Americas, discussions are underway on the feasibility of extending this to inter-coastal shipping in the Americas, and possibly other modes of transportation. The decision whether to proceed with such a project may depend on the extent of Latin American participation in a second project initiated this year, discussed below.

CMI and UNCITRAL: Rules for international bills of lading, liability and other matters for ocean carriage of goods by sea.

The Comité Maritime International (CMI) in Brussels and UNCITRAL have cooperated, along with the Maritime Law Associations of a number of countries, in preparing draft approaches to a new effort to unify the long-fractured field of rules on carriage of goods by sea. UNCITRAL approved the project last month, and scheduled the first meeting for the Spring 2002, which would have on the table a draft convention prepared by CMI which is expected to be distributed for comment in December 2001. The U.S. has maintained that such a project should include all issues covered by standard bill of lading laws, and not be limited to liability standards or limits, as have some earlier international efforts, a position upheld at UNCITRAL.

The new project will not be aimed at multimodal shipping, although this is not ruled out at a later stage. Other bodies continue in separate projects to seek multimodal rules, such as UNCTAD and the UNECE, but this approach was rejected by the U.S. and others as an unreachable goal at this stage, since it would require cooperation of the other modes such as rail and road, as well as their respective industries and users.

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An opportunity for broader harmonization presents itself for the U.S., in that concurrently new COGSA legislation drafted by the MLA may be introduced in Congress to amend domestic U.S. maritime law on this subject, and the corresponding provisions of the UCC (Article 7 on bills of lading) are now also being considered for revision. This will permit both domestic and international legal issues – which are becoming increasingly hard to separate – to be on the table, which can be beneficial to import-export, shipping and transportation finance interests if wider harmonization occurs.

Commercial dispute resolution

While a separate topic which will be covered in other reports, it is referred to briefly here because of its importance to commercial and transactional law, and because harmonization has been sought in the same international bodies.

Hague Conference: Draft convention on jurisdiction and enforcement of judgments.

The draft judgments convention, which includes proposed rules on jurisdiction, is moving toward a decision point next January at the Hague as to whether it will proceed, and whether the U.S. is able to support it. Intercessional meetings are continuing in an effort to seek consensus on core issues and to build out from that, rather than focus first on the EU's Brussels/Lugano treaty system as the starting point, which has not been acceptable to the U.S., ATLA and others. In addition, U.S. led efforts continue on seeking appropriate coverage for electronic commerce and related intellectual property cases, which present difficult challenges not on the table at the time this project started years ago. Outside of this project, the U.S. is not a party to any bilateral or multilateral agreements on enforcement of judgements, as contrasted with U.S. participation

in the widely adopted UN New York Convention on foreign arbitral awards and the OAS Panama convention on commercial arbitration.

UNCITRAL: International commercial arbitration

The Working Group on Arbitration has begun work this year on model legislative provisions on conciliation, enforceability of interim awards and measures of protection, enforceability of awards set aside in the state of origin, and interpretations of the New York Convention on Foreign Arbitral Awards so that treaty requirements for written arbitration agreements are satisfied by electronic communications. Meetings will be held in Vienna and New York in November 2001 and the Spring of 2002.

UNIDROIT and ALI: Joint project on rules for dispute resolution

The joint project continues its effort to merge civil law and common law approaches to dispute resolution, which could lessen the burden of cross-border cases and reduce conflict in arbitration and other ADR cases where basic rules of procedure are often in dispute. The status of this project will be reviewed this September at the UNIDROIT meeting of its Governing Council.

Note: Participation by ABA members through their Sections is welcomed on all projects; sites for or copies of documents will be made available on request.